

Message Text

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ACTION EUR-12

INFO OCT-01 ISO-00 SP-02 AID-05 EB-07 NSC-05 CIEP-01

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R 241704Z SEP 75

FM AMEMBASSY OTTAWA

TO SECSTATE WASHDC 7600

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POUCHED AS INFO TO ALL CONSULATES IN CANADA

E.O. 11652: N/A

TAGS: EFIN, ECON, CA

SUBJ: WILL CONCERN OVER INFLATION LEAD TO WAGE AND PRICE
CONTROLS?

1. SUMMARY. THIS CABLE REVIEWS AND COMMENTS ON CURRENT
DEBATE IN CANADA ON INFLATION AND HOW TO CONTROL IT AND
SUMMARIZES BANK OF CANADA GOVERNOR BOUEY'S SEPTEMBER 22
SPEECH DEFENDING ACTIONS TO LIMIT GROWTH OF MONEY SUPPLY.
END SUMMARY.

2. PRESSURES BEGINNING MOUNT AGAIN WITHIN CANADA FOR SOME
TYPE OF WAGE AND PRICE CONTROLS WITH RETURN OF DOUBLE-DIGIT
INFLATION LEVELS. (CPI ROSE 1.0 PERCENT IN AUGUST AND WAS
11.1 PERCENT ABOVE AUGUST 1974. ON SEASONABLY ADJUSTED BASIS,
CPI'S LATEST THREE-MONTH COMPOUND PERCENTAGE CHANGE AT ANNUAL
RATES WAS 13.9 PERCENT OR ROUGHLY SIMILAR TO EXTREMELY HIGH
RATE OF INFLATION EXPERIENCED IN LATTER PART OF 1974).
CONFERENCE BOARD OF CANADA RECENTLY REVISED ITS PRO-
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JECTIONS FOR CANADIAN ECONOMY, FORECASTING 11.1 PERCENT

INCREASE IN CPI FOR 1975 AND 11.5 PERCENT FOR 1976.

3. BANKS AND FINANCIAL INSTITUTIONS IN RECENTLY PUBLISHED REPORTS HAVE STRESSED INFLATION AS MAJOR ECONOMIC PROBLEM BUT MOST HAVE SUGGESTED GOVERNMENT FISCAL RESTRAINT RATHER THAN WAGE AND PRICE CONTROL MECHANISM AS SOLUTION TO PROBLEM. HOWEVER, NUMBER OF ECONOMISTS AND ANALYSTS PREDICTING DIRE ECONOMIC CONSEQUENCES IF GOC DOES NOT MOVE STRONGLY TO CURB INFLATION APPEARS ON INCREASE.

4. ANDRE RAYNAULD, CHAIRMAN OF ECONOMIC COUNCIL OF CANADA, RECENTLY ADDED COUNCIL'S WEIGHT TO THOSE CALLING FOR DRACONIAN MEASURES TO FIGHT INFLATION. AS REPORTED IN LOCAL PRESS, RAYNAULD PROPOSED IMPOSITION OF SURTAX ON LARGE WAGE AND PRICE INCREASES. NEWS-PAPERS OF SEPTEMBER 22 QUOTED RAYNAULD AS SAYING COUNCIL HAS TENTATIVELY PROPOSED SURTAX ON WAGE AND PROFIT INCREASES THAT EXCEED 10 PERCENT. HE REPORTEDLY ACKNOWLEDGED THAT FORMER FINMIN TURNER HAD REJECTED SURTAX IDEAS AS "AN ADMINISTRATIVE MONSTER."

5. FORMER DEPUTY FINANCE MINISTER SIMON REISMAN WAS QUOTED IN PRESS OF SEPTEMBER 17 AS CALLING FOR NATIONAL PRICE-AND-WAGE "FREEZE" IN ORDER TO "BREAK THE ATMOSPHERE OF EXPECTATIONS. AND IT MUST BE REINFORCED BY FISCAL AND OR MONETARY CONTROLS." TORONTO STAR OF SEPTEMBER 15 AND GLOBE AND MAIL OF SEPTEMBER 18 CONCLUDED THAT SENIOR OFFICIALS IN FINANCE DEPARTMENT WERE EXPECTED TO TAKE SAME LINE WITH TURNER'S REPLACEMENT AND ADVISE HIM THAT CONTROLS WERE PREFERRED GOC POLICY OPTION.

6. ON SEPTEMBER 22 BANK OF CANADA GOVERNOR GERALD BOUEY OUTLINED BANK'S RESTRICTIVE MONETARY POLICY FOR NEAR-TERM. SPEAKING TO CANADIAN CHAMBER OF COMMERCE AT SASKATOON, BOUEY DEFENDED RECENT INCREASE OF .75 PERCENT IN BANK RATE TO 9 PERCENT ON INFLATION-FIGHTING GROUNDS. DECISION, ACCORDING TO BOUEY, WAS BASED ON NEED TO PROTECT "VALUE OF MONEY" AND "TO KEEP THE RATE LIMITED OFFICIAL USE

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OF MONETARY EXPANSION WITHIN REASONABLE LIMITS."

7. BOUEY DESCRIBED BANK'S ACTION IN RAISING BANK RATE IN TERMS OF RECENT GROWTH IN MONEY STOCK, WHICH "ACCELERATED TO RATES OF IN EXCESS OF 20 PERCENT A YEAR -- RATES WHICH, IF ALLOWED TO CONTINUE, WOULD LEAD IN DUE COURSE TO AN ACCELERATION OF THE RATE OF INFLATION IN CANADA. IN THESE CIRCUMSTANCES, THE

CENTRAL BANK HAD NO RESPONSIBLE ALTERNATIVE BUT TO LET MARKET INTEREST RATES MOVE UPWARD IN RESPONSE TO THE PRESSURE OF CREDIT DEMANDS, AND TO ADJUST ITS OWN LENDING RATE ACCORDINGLY."

8. SPEAKING OF ECONOMY IN GENERAL, ?9736 5-53\$ 5#-5

"THERE IS ACCUMULATING EVIDENCE THAT THE WROST OF THE RECESSION MAY NOW BE BEHIND US AND THAT PRODUCTION IS BEGINNING TO RECOVER." HOWEVER, BOUEY CONCENTRATED MAJORITY OF HIS REMARKS ON INFLATION PROBLEM AND ITS DIRE CONSEQUENCIES FOR CANADA.

9. BOUEY BLAMED CURRENT WAVE OF INFLATION ON "SHORT BUT INTENSE BOOM" IN CANADA "THAT GAVE RISE TO DEMANDS FOR HIGHER RATES OF INCREASE IN LABOUR INCOMES. BOOM ENDED SOME TIME AGO", SAID BOUEY, "AND NEW WAGE AND SALARY SETTLEMENTS CONTINUE TO BE DISTRUBINGLY LARGE."

10. BOUEY ALSO QUESTIONED CONVENTIONAL WISDOM OF "ALMOST EVERY COUNTRY IN THE WESTERN WORLD" WHICH "HAS GIVEN RAPID GROWTH AND HIGH EMPLOYMENT MUCH HIGHER PRIORITY IN ITS POLICIES THAN THE PRESERVATION OF THE VALUE OF MONEY." SUCH POLICY "WON'T WORK WELL ANY LONGER. THE LOSS OF CONFIDENCE IN THE VALUE OF MONEY THAT HAS RESULTED FROM THESE POLICIES HAS NOW BECOME SO GREAT ALMOST EVERYWHERE AS TO THREATEN THE EFFECTIVE FUNCTIONING OF OUR EXISTING ECONOMIC, SOCIAL AND POLITICAL INSTITUTIONS. WE NOW HAVE NO OPTION BUT TO CONTAIN INFLATION AND INFLATIONARY EXPECTATIONS..."

11. COMMENT: FORMER FINMIN TURNER SAID DURING BUDGET SPEECH OF LAST JUNE 23 THAT CANADIAN PEOPLE WERE NOT READY FOR WAGE AND PRICE CONTROLS AND THAT PUBLIC LIMITED OFFICIAL USE

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ATTITUDE WAS A MAJOR FACTOR IN GOC'S DECISION NOT IMPOSE CONTROLS THEN. WITH MORE AND MORE CANADIAN ECONOMISTS AND PUBLIC FIGURES STRESSING IMPORTANCE OF STOPPING INFLATIONARY SPIRAL AND CONTINUED EROSION OF PURCHASING POWER OF CANADIAN DOLLAR, CANADIAN PUBLIC MAY BE CLOSER TO ACCEPTING SOME FORM OF CONTROLS NOW THAN LAST SPRING.

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ACTION EUR-12

INFO OCT-01 ISO-00 SP-02 AID-05 EB-07 NSC-05 CIEP-01

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12. IMPORTANT FACTOR IN ASSESSING MOOD OF CANADIAN PUBLIC TOWARD CONTROLS AND POSSIBLE GOC ACTIONS THIS REGARD IS CANADIAN ECONOMIC POSITION VIS-A-VIS U.S. CONTINUED DEFICIT IN TRADE BALANCE WITH U.S., LOWERED VALUE OF CANADIAN DOLLAR IN EXCHANGE FOR U.S. COUNTERPART, SMALLER INCREASES IN INFLATION RATE SOUTH OF BORDER AND CONSTANT REPETITION BY POLITICIANS AND ANALYSTS THAT CANADIAN GOODS ARE BECOMING NON-COMPETITIVE DUE EXCESSIVE WAGE SETTLEMENTS HAVE DISSIPATED EUPHORIA THAT EXISTED HERE ABOUT YEAR AGO REGARDING CANADA'S "FAVORED" POSITION IN REGARD TO OTHER INDUSTRIAL COUNTRIES, PARTICULARLY U.S.

13. WITH RESIGNATION OF TURNER AND NO IMMEDIATE REPLACEMENT, THERE SEEMS VACUUM IN GOC ECONOMIC POLICY. LAST WEEK'S CABINET MEETING, WHICH REPORTEDLY CONCENTRATED ON ECONOMIC PROBLEMS, PRODUCED NO INDICATION OF GOC FISCAL POLICY DIRECTION. UNTIL FINANCE MINISTER WITH DEFINITE PLANS FOR GOC ECONOMIC POLICY

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IS APPOINTED (AND PERHAPS BRINGS DOWN NEW BUDGER WITH SPECIFIC PROPOSALS), GOC POLICY WILL BE MADE ON AD HOC

BASIS, AND WAGE AND PRICE CONTROLS OR ANY OTHER IMPORTANT ECONOMIC POLICY DECISION WILL BE DEFERRED.

14. ADDITIONALLY, POLITICAL CONSIDERATIONS MAY BE IMPORTANT FACTOR IN TRUDEAU'S DECISION WHETHER OR NOT GO WAGE/PRICE CONTROL ROUTE. (ALTHOUGH ONE POLITICAL CARTOONIST RECENTLY INDICATED THAT SITUATION WAS SO BAD THAT MARGARET MAY HAVE ANOTHER BABY.)

15. OPTING FOR CONTROLS, HOWEVER LIMITED, SHOULD EASE GROWING CRITICISM OF TRUDEAU ADMINISTRATION ON LACK OF LEADERSHIP AND FAILURE "DO SOMETHING" TO CURE INFLATIONARY SPIRAL. TURNER'S RESIGNATION HAS BEEN WIDELY ATTRIBUTED TO HIS FAILURE TO CONVINCE HIS CABINET COLLEAGUES (READ TRUDEAU) TO TAKE "TOUGH MEASURES" TO COPE WITH INFLATION (SEE OTTAWA 3480). NOTHING IN TURNER'S PUBLIC STATEMENTS OVER PAST FEW MONTHS SHOW HE HAD SWITCHED TO ADVOCACY OF WAGE/PRICE CONTROLS, AND, IN FACT, STATEMENT BY RAYNAULD REGARDING TURNER'S REJECTION OF SURTAX PROPOSAL AS CREATING "BUREAUCRATIC MONSTER" WOULD INDICATE TURNER'S CONTINUED PREFERENCE FOR MUCH TOUGHER FISCAL RESTRAINT IN LIEU OF RIGID CONTROL SYSTEM. HOWEVER, TURNER WAS SERIOUSLY CONCERNED ABOUT HIGH WAGE SETTLEMENTS IN CANADA PRICING CANADA'S GOODS OUT OF INTERNATIONAL MARKETS, AND HE MUST HAVE BEEN THINKING OF SOME MECHANISM TO BRING SETTLEMENTS UNDER CONTROL (IN JUNE BUDGET SPEECH HE WARNED THAT GOC WOULD BE PREPARED TO ACCEPT STRIKES IN PUBLIC SERVICE SECTOR RATHER THAN ACQUIESCE TO "UNWARRANTED" WAGE DEMANDS).

16. ADVOCACY OF WAGE/PRICE CONTROLS BY PROGRESSIVE CONSERVATIVES IN 1974 WAS ATTACKED AT THE TIME BY LIBERALS AND IS REPORTEDLY ONE OF ISSUES WHICH HELPED ELECT THEM. TO GO FOR CONTROLS NOW AGAINST THIS BACKGROUND COULD LEAVE TRUDEAU OPEN TO CHARGES OF LACK OF FORESIGHT, MISMANAGEMENT OF ECONOMY FOR DOCTRINAL/PARTISAN POLITICAL MOTIVES, AND NEEDLESS PROVOCATION OF TURNER'S RESIGNATION TO DETRIMENT OF LIMITED OFFICIAL USE

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LIBERAL PARTY UNITY (WITH OVERTONES OF INCREASINGLY ACRIMONIOUS LANGUAGE IF ANGLOPHONE TURNER REPLCED BY FRANCOPHONE).

17. TRUDEAU HAS UNDOUBTEDLY BEEN HOPING THAT RESURGENCE OF U.S. ECONOMY WOULD BE REFLECTED IN UPTURN IN CANADA IN TIME TO SPARE HIM NEED TO TAKE TOUGH DECISION. HOWEVER, IF ECONOMY FAILS EXPAND MORE RAPIDLY, INFLATION RATES INCREASE, AND EVIDENCE OF PUBLIC ACCEPTABILITY

OF CONTROLS MOUNTS, TRUDEAU MAY DECIDE TO GIVE HIS
POLITICAL OPPOSITION THEIR FIELD DAY FOR CRITICIZING
HIM AND PROVIDE HIS LEADERSHIP CONTENDER TURNER WITH
AN ACCRUAL OF POLITICAL CAPITAL BY INSTITUTING SOME
FORM OF CONTROLS.

18. IF TRUDEAU DOES DECIDE ON CONTROLS, HIS POLICY
OPTIONS RANGE FROM "FREEZE" (AS PROPOSED BY REISMAN)
TO MINIMAL ACTION WAGE/PRICE BOARD, WHICH WOULD SET
GUIDELINES BUT HAVE NO PENALTY POWER. LOGICALLY,
TRUDEAU SHOULD REACT TO MOUNTING CRITICISM AND INSTITUTE
SOME CONTROL MECHANISM, EVEN IF IT IS OF LATTER TYPE
WHICH WAS ONLY marginally SUCCESSFUL IN EARLY 70'S.
POSITIVE DECISION ON CONTROLS WOULD PROVIDE TRUDEAU
WITH OPPORTUNITY TO DEMONSTRATE HE STILL IN COMMAND
AND GET ECONOMIC ISSUES IN FOCUS BEFORE HE IS FACED
WITH POSSIBILITY OF AN ELECTION OR OF LIBERAL PARTY
LEADERSHIP CONVENTION.
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Message Attributes

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Draft Date: 24 SEP 1975
Decaption Date: 01 JAN 1960
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Authority: SmithRJ
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 28 MAY 2004
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
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